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In the Supreme Court of the United States

OCTOBER TERM, 1948

Nos. 767 and 768

BREEDING MOTOR FREIGHT LINES, INC., DEBTOR,

and

BREEDING MOTOR COACHES, INC., DEBTOR, PETITIONERS,

v.

RECONSTRUCTION FINANCE CORPORATION

Nos. 769 and 770

GLENN E. BREEDING AND IRENE BREEDING, DOING BUSINESS AS BREEDING MOTOR COACHES AND BREEDING MOTOR FREIGHT LINES, BREEDING MOTOR FREIGHT LINES, INC., AND BREEDING MOTOR COACHES, INC., PETITIONERS

v.

RECONSTRUCTION FINANCE CORPORATION

ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The order of the District Court for the Eastern District of Oklahoma in Nos. 767 and 768 (767 R.

389-390),[1] its order in No. 769 (767 R. 274-278) and its finding of fact and order in No. 770 (770 R. 85-89) were entered without opinions. The opinion of the Court of Appeals for the Tenth Circuit (767 R. 871-885; 770 R. 109-123) is reported at 172 F. 2d 416.

JURISDICTION

The judgment of the Court of Appeals was entered on February 7, 1949 (767 R. 886; 770 R. 124). The petitions for writs of certiorari were filed on May 6, 1949. The jurisdiction of this Court is invoked under 28 U. S. C. 1254(1).

QUESTIONS PRESENTED

(1) Whether the reorganization petitions were properly dismissed as lacking good faith within the meaning of Chapter X of the Bankruptcy Act.

(2) Whether the foreclosure sale, made pursuant to 28 U. S. C. 2001(a), should be set aside for alleged irregularities.

(3) Whether the foreclosure judgment, on which the sale was based, should be vacated because the mortgage agreement was not approved in advance by the Interstate Commerce Commission as required by Section 20(a) of the Interstate Commerce Commission Act (41 Stat. 494).

STATUTES INVOLVED

The pertinent statutory provisions are set forth in the Appendix, *infra,* pp. 14-16.

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[1] There are two records involved in these four connected cases; the record in Nos. 767-768-769 is referred to as 767 R.; the record in No. 770 is referred to as 770 R.

STATEMENT

These four cases arise out of the insolvency of Glenn E. and Irene Breeding, doing business as common carriers by motor under the names of Breeding Motor Freight Lines and Breeding Motor Coaches, and of their two wholly-owned corporations, successors to their partnership business, Breeding Motor Freight Lines, Inc., and Breeding Motor Coaches, Inc. All of these parties are referred to as petitioners, except where otherwise stated, since the activities on behalf of all of them were carried on by Glenn E. Breeding.

Respondent had agreed in November 1945 to lend petitioners $560,000, repayable in monthly installments of $9,334.00. Respondent had advanced over half of the loan, but petitioners defaulted on the second installment, due January 9, 1946. The first legal proceedings in this case were instituted on February 1, 1946, when the respondent filed suit in the district court for judgment upon petitioners' promissory note and for foreclosure of real and chattel mortgages securing the note [2] (767 R. 1-5). Petitioners filed an answer and counterclaim to the foreclosure action alleging

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[2] The petitioner corporations were organized at the time of the loans, but since Interstate Commerce Commission's approval of the transfers of operating rights from the partnership to them was necessary, the transfers were not completed until July, 1946 (767 R. 499). The corporations were subsequently made parties to the foreclosure action (767 R. 192-193). Two junior mortgagees were named as parties defendant, and the United States and the State of Oklahoma intervened for tax claims (767 R. 193-197).

that the respondent should have made a second advance to them before their second installment on the debt was due (767 R. 51-53). However, at the hearing on April 15, 1946, the attorneys for petitioner and respondent agreed that petitioners would drop their claim and confess judgment for the principal amount due; that the receiver appointed on the filing of the suit was to be discharged; and that Mr. Breeding was to have possession of the business for 60 days during which time he would try to salvage it, but if he could not do so, then the mortgaged property was to be sold by a Special Master to be appointed by the district court (767 R. 101-102). Judgment for respondent and the other mortgagees, including a decree of foreclosure sale on these terms, was entered the same day (767 R. 154-162).

Petitioner stayed in possession until May 2, 1947, when a Special Master was appointed to sell the property (767 R. 198). On May 29, 1947, Breeding Motor Freight Lines, Inc., filed a petition in the district court for a stay of the foreclosure proceedings and for a reorganization under Chapter X of the Bankruptcy Act (767 R. 321-340). Two days later, on May 31, a similar petition was filed on behalf of Breeding Motor Coaches, Inc. (767 R. 395-406). The two petitions were consolidated and after a hearing (767 R. 464-613) were dismissed by the district court on June 10, 1947, on the finding that the petitions had not been

filed in good faith as required by Chapter X of the Bankruptcy Act (767 R. 389-390).

Proceedings on the foreclosure sale were brought to a conclusion. On June 27, 1947, the Special Master secured a new execution and order of sale to take into account changes since April 15, 1946 (767 R. 199, 203-206); petitioners' objections to the Special Master's notice of sale (767 R. 207-218) were overruled on August 11, 1947 (767 R. 219); the sale, by public auction, was held on August 18, 1947; and the next day the Special Master filed his return together with a transcript of the sale proceedings, showing that all the property was purchased by respondent (767 R. 219-261). Petitioners objected to confirmation of the sale (767 R. 262-272), and after a hearing (767 R. 280-303) the district court confirmed the sale on September 8, 1947 (767 R. 274).

The property included certain operating rights granted by the Interstate Commerce Commission which respondent resold to other carriers. The purchasers of these operating rights applied for the necessary approval, and on May 28, 1948, the Interstate Commerce Commission approved the transfers of the rights from the Special Master to the purchasers (770 R. 18-62). Petitioners appeared in these proceedings before the Interstate Commerce Commission and objected on the ground that their foreclosed securities had not been approved by the Commission. The Commission held

that this was a collateral attack on a final judicial sale which it would not consider (770 R. 28).

On June 14, 1948, over two years after the original judgment, petitioners filed a motion in the district court to vacate the judgment and to set aside the foreclosure sale on the ground that the note and mortgages involved were void for lack of approval by the Interstate Commerce Commission (770 R. 15-16). Upon both a hearing (770 R. 91-105) and stipulated facts (770 R. 76-84), the district court on August 21, 1948, entered its findings of fact, conclusions of law, and order dismissing the motion to vacate the foreclosure judgment (770 R. 85-89). The district court held that petitioners were inexcusably late in making this defense to the foreclosure and that the equities were against them (770 R. 87).

All these proceedings in the district court were heard and decided by District Judge Rice. Petitioners appealed from the decisions of the district court dismissing the reorganization petitions, confirming the foreclosure sale, and dismissing the motion to vacate. The Court of Appeals for the Tenth Circuit upheld each of these decisions (767 R. 886-887; 770 R. 124).[3] The dismissal of

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[3] Respondent appealed from the findings of the district court that the loan to petitioner was in excess of $500,000 and thus subject to Interstate Commerce Commission's approval (770 R. 86). That appeal was denied by the Court of Appeals on the ground that the finding was not an appealable final order or judgment (767 R. 885; 770 R. 123). That issue is not before this Court.

the reorganization petitions is involved in Nos. 767 and 768; the confirmation of the foreclosure sale is involved in No. 769; and the motion to vacate the foreclosure judgment is involved in No. 770.

ARGUMENT

(1) As both courts below found, petitioners' motor freight and passenger business, at the time of the filing of petitions for reorganization under Chapter X of the Bankruptcy Act, was hopelessly insolvent, and there was no reasonable possibility of successful operations. Petitioners had acquired the business in 1944. They suffered substantial losses from its inception. Throughout the history of the venture, their constant plan to save the business was to sell some routes, property and equipment, and, with the further help of loans, to purchase new equipment (767 Pet. 24). But, except for two items, they never could sell the surplus properties, or meet existing debts or overcome mounting operating losses (767 R. 576-579). By May, 1947, any salvage plan had become impossible of realization.

Operating losses were excessive.[4] The judgment secured by mortgage to respondent and the

[4] The net operating loss for 1946 for the Motor Coaches was $77,578 on a gross revenue of $89,173; and for the first four months of 1947 the loss was $30,821.57 on a gross revenue of $14,915.97. The net operating loss upon the Freight Lines for 1946 was $189,410 on a gross revenue of $408,297.00; and for the first four months of 1947 the net operating loss was $44,533 on a gross revenue of $153,123.53 (767 R. 866-869). Thus, the average monthly loss for both operations in 1947

other mortgagees totaled $421,547.52, exclusive of interest, and attorneys' fees.[5] There were other lien claims. Petitioners had used for operating expenses $20,000 of C.O.D. collections (767 R. 578); $100,000 of various federal taxes collected from the source (767 R. 195);[6] and nearly $2,000 of Oklahoma sales taxes collected on fares. In addition, $10,000 was due the state for mileage taxes. Both federal and state tax liens had been filed. (767 R. 193-196.) Petitioners owed $10,000 on inter-line accounts (767 R. 577). In addition to the judgment debt, they owed respondent another $21,250 for advances made to cover operating expenses (767 R. 578). There was a debt of $52,000 to unsecured creditors, and the individual petitioners personally owed $67,000 on partnership notes (767 R. 579). The business had been shut down for lack of cash to pay wages (767 R. 522), some of the state operating rights had been cancelled, and proceedings were pending before the Interstate Commerce Commission to cancel rights issued by it (767 R. 591). Petitioners had no cash (767 R. 578).

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before interest and depreciation, was $18,838 on a gross monthly income of only $42,000.

[5] This sum includes $253,577.52 due to respondent on the original note (767 R. 155), plus $42,250 advanced during 1946 and added to the judgment (767 R. 191); $77,720 due to one mortgagee and $48,000 due to the other (767 R. 157).

[6] Petitioners say that these tax claims were being compromised (Pet. 767, p. 24), but the only evidence is that Mr. Breeding had made an offer on which the federal tax authorities had not acted (767 R. 598).

To meet this picture, petitioners rely upon a valuation by Mr. Breeding of the property, item by item (Pet. 767, p. 23-24). This valuation (767 R. 645-654) is irrelevant for reorganization purposes, since the business was not a profitable one. *Consolidated Rock Co.* v. *Du Bois,* 312 U. S. 510, 525-526. To put it on a profitable basis, Mr. Breeding acknowledged that he would need a new loan of $360,000 (767 R. 597). To secure these funds, petitioners had some vague plans for selling some portions of the properties and for issuing receiver certificates (767 R. 602-605). At the time of the hearing, petitioners were asking respondent for working cash (767 R. 601).

In the face of these facts, the action of the district court dismissing the petitions for reorganization was not only within its discretion (*Tennessee Publishing Co.* v. *American National Bank,* 299 U. S. 18; *Manati Sugar Co.* v. *Mock,* 75 F. 2d 284 (C. A. 2); *Brockett* v. *Winkle Terra Cotta Co.,* 81 F. 2d 949 (C.A. 8); *Chapman Bros. Co.* v. *Security-First National Bank of Los Angeles,* 111 F. 2d 86 (C.A. 9); *San Francisco Laundry Ass'n* v. *American Trust Co.,* 127 F. 2d 187 (C.A. 9)); retention of these reorganization proceedings would have been an error on the part of the district court. *Fidelity Assurance Ass'n* v. *Sims,* 318 U. S. 608; *Provident Mut. Life Ins. Co. of Philadelphia* v. *University Evangelical Lutheran Church of Seattle,* 90 F. 2d

992 (C. A. 9); *First Nat. Bank of Wellston* v. *Conway Road Estates Co.*, 94 F. 2d 736 (C. A. 8), certiorari denied, 304 U. S. 578; *Price* v. *Spokane Silver & Lead Co.*, 97 F. 2d 237 (C. A. 8); *In re Suburban Properties, Inc.*, 110 F. 2d 438 (C. A. 7); *In re Sheridan View Bldg. Corporation*, 149 F. 2d 532 (C. A. 7). No feasible plan, which the secured creditors could have been forced to accept, was possible. Cf. *Case* v. *Los Angeles Lumber Products Co., Ltd.*, 308 U. S. 106, 109.[7]

2. The objections to the foreclosure sale presented to this Court in No. 769 are groundless. The sale was conducted in substantial accord with the order of sale and pursuant to 28 U. S. C. 2001(a) (767 R. 275-276); it was attended by at least seven of the reputable motor carriers in the area (767 R. 300), and there was spirited bidding on each parcel of property (767 R. 241-261). Petitioners' objections go to technical, minute details; they do not show that any bidders were misled or that any higher bids for the property could have been obtained from any source. Petitioners argue, first, that there is a shocking discrepancy between the sale price of $145,000 and the petitioners' own valuation of $913,000, which, taken with alleged irregularities, proves that prejudicial errors were com-

[7] Since the plan was not feasible, the creditors' objections thereto are in good faith. Section 203 of Chapter X of the Bankruptcy Act, authorizing the disregard of objections not in good faith, consequently does not apply, and *Young* v. *Higbee Co.*, 324 U. S. 204, which involved such objections, cited by petitioners (Pet. No. 767, p. 25), is irrelevant.

mitted (767 Pet., pp. 33-34). But there is no shocking discrepancy, because petitioners' valuation is too high, and the price received is not low. Petitioners' valuation of an insolvent business as if it were a going concern is no measure of its value, *Consolidated Rock Co.* v. *Du Bois, supra,* p. 9, and the price which property commands at a forced sale "may be hardly even a rough measure of its value." *Gelfert* v. *National City Bank,* 313 U. S. 221, 233. Petitioners' expert witness in the reorganization petition hearings testified that at a public sale the property could not be expected to bring in more than 25% of its value (767 R. 491).

Petitioners argue, alternatively, that no affirmative showing of prejudice is required to set aside a sale for irregularities (767 Pet. 35). But the rule is clear that the irregularities must themselves be of such a nature as to be prejudicial to a fair sale, or else an affirmative showing of prejudice must be made. *Pewabic Mining Company* v. *Mason,* 145 U. S. 349. The cases cited by petitioner do not support its argument. In the *Pewabic Mining Co.* case, the court refused, in the absence of an affirmative showing of prejudice, to set aside a sale for trifling errors. See also *Stockmeyer* v. *Tobin,* 139 U. S. 176, 196. In *Schroeder* v. *Young,* 161 U. S. 334, there was fraud. In *Ballentyne* v. *Smith,* 205 U. S. 285, 291, both the commissioner who made the sale and the district court, familiar with local conditions, refused to confirm the sale, because the price

was so grossly inadequate. In *Gelfert* v. *National City Bank, supra,* there was a statute fixing a minimum upset price.

Petitioners cite *Bovay* v. *Townsend,* 78 F. 2d 343 (C. A. 8), as being in conflict with the decision below on the point of prejudice (767 Pet., p. 35). But in that case, the fact of an unfair sale was, in the court's judgment, inherent in the method of sale. Bridges located in two different places, serving two different communities, should have been sold separately. That case obviously rested on its peculiar facts and is no authority for the proposition asserted here, that, as a matter of law, the bulk sale of the operating equipment of a single enterprise, including miscellaneous items of office furniture, is bound to bring a substantially lower price than a sale of each item separately. This is an unsupportable contention. *Reconstruction Finance Corp.* v. *Kentucky River Coal Corp.,* 114 F. 2d 942 (C. A. 6).

3. The motion to vacate the foreclosure judgment presents no reviewable issue to this Court. The statutes, *infra,* pp. 15-16, requiring approval by the Interstate Commerce Commission of the issuance of securities by a carrier subject to its regulation were enacted to prevent financial manipulation by those in control of the carrier. *New York, Chicago & St. Louis R. R. Co.* v. *Frank,* 314 U. S. 360. The validity of the securities cannot be questioned collaterally and late, at the instance of petitioners who benefited from the original transaction,

to upset a final orderly liquidation of an insolvent enterprise. *New York, Chicago & St. Louis R. R. Co.* v. *Frank, supra; Guaranty Trust Co. of N. Y.* v. *Minneapolis & St. Louis R. R. Co.*, 36 F. 2d 747 (C. A. 8); *Marony* v. *Wheeling & L. E. Ry. Co.*, 33 F. 2d 916 (S. D. N. Y.).

CONCLUSION

The decisions below rest upon the peculiar facts of the case and are correct. No important questions of law and no conflict of decisions are involved. We respectfully submit that the petition for a writ of certiorari should be denied.

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JUNE 1949

APPENDIX

I

Chapter X of the Bankruptcy Act, 52 Stat. 883, 887, 11 U.S.C. 541, 546, provides in relevant part as follows:

> ARTICLE VI—APPROVAL OR DISMISSAL OF PETITION
>
> SEC. 141. Upon the filing of a petition by a debtor, the judge shall enter an order approving the petition, if satisfied that it complies with the requirements of this chapter and has been filed in good faith, or dismissing it if not so satisfied.
>
> SEC. 146. Without limiting the generality of the meaning of the term "good faith", a petition shall be deemed not to be filed in good faith if—
>
> * * * * *
>
> (3) it is unreasonable to expect that a plan of reorganization can be effected;
>
> * * * * *

II

28 U.S.C. Sec. 2001(a) provides in relevant part as follows:

> § 2001. Sale of realty generally
>
> (a) Any realty or interest therein sold under any order or decree of any court of the United States shall be sold as a whole or in separate parcels at public sale at the courthouse of the county, parish, or city in which the greater part of the property is located, or upon the premises or some parcel thereof lo-

cated therein, as the court directs. Such sale shall be upon such terms and conditions as the court directs.

* * * * *

III

Interstate Commerce Act, 41 Stat. 456, 494 (49 U. S. C. 20(a)) provides in relevant part as follows:

SEC. 20a. * * *

(2) * * * it shall be unlawful for any carrier to issue any share of capital stock or any bond or other evidence of interest in or indebtedness of the carrier (hereinafter in this section collectively termed 'securities') * * * unless and until, and then only to the extent that, upon application by the carrier, and after investigation by the Commission of the purposes and uses of the proposed issue and the proceeds thereof, * * * the Commission by order authorizes such issue or assumption. The Commission shall make such order only if it finds that such issue or assumption: (a) is for some lawful object within its corporate purposes, and compatible with the public interest, which is necessary or appropriate for or consistent with the proper performance by the carrier of service to the public as a common carrier, and which will not impair its ability to perform that service, and (b) is reasonably necessary and appropriate for such purpose.

* * * * *

(11) Any security issued or any obligation or liability assumed by a carrier, for which

under the provisions of this section the authorization of the Commission is required, shall be void, if issued or assumed without such authorization therefor having first been obtained, * * *. In case any security so made void was directly acquired from the carrier issuing it the holder may at his option rescind the transaction and upon the surrender of the security recover the consideration given therefor. Any director, officer, attorney or agent of the carrier who knowingly assents to or concurs in any issue of securities or assumptions of obligation or liability forbidden by this section, or any sale or other disposition of securities contrary to the provisions of the Commission's order or orders in the premises, or any application not authorized by the Commission of the funds derived by the carrier through such sale or other disposition of such securities, shall be guilty of a misdemeanor and upon conviction shall be punished by a fine of not less than $1,000 nor more than $10,000, or by imprisonment for not less than one year nor more than three years, or by both such fine and imprisonment in the discretion of the court.

* * * * *

IV

Motor Carrier Act, as amended, 52 Stat. 1240 (49 U.S.C. 314) provides in relevant part as follows:

> SEC. 214. Common or contract carriers by motor vehicle * * * shall be subject to the provisions of paragraphs 2 to 11, inclusive, of section 20(a) of part I of this Act * * *.

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